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978-1-107-02744-2 - Availability of Credit and Secured Transactions in a Time of Crisis

Edited by N. Orkun Akseli

Excerpt

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## Introduction

N. ORKUN AKSELI

This collection of essays emanates from a conference – *International Legal Standards on Secured Transactions, Facilitation of Credit and Financial Crisis* – sponsored by the World Bank, funded by the *Modern Law Review* Seminar Funds and hosted by Newcastle University Law School in May 2010. That conference addressed the challenges posed by inefficient secured credit laws and explored the avenues to overcome these difficulties by examining the international legal standards set by international financial institutions and international legislative bodies.<sup>1</sup>

This collection, along the same lines, assesses the challenges posed by inefficient secured credit laws by looking at how challenges can be overcome to facilitate credit through legal reforms based on international standards set by international legislative bodies and financial institutions in the light of the financial crisis. The collection focuses particularly on the legislative texts prepared by the United Nations Commission on International Trade (UNCITRAL), and harmonization and modernization initiatives by the World Bank and the European Bank for Reconstruction and Development (EBRD). The collection deals with key issues such as the availability of credit, international financial institutions and their involvement in secured transactions law reform, utility and efficacy of the UNCITRAL's legislative efforts, and the extent to which these international standards set by international standard-setting bodies and financial institutions may be used to help reform the law of credit and security.

Since the early 1970s, an increasing variety of international conventions and instruments on secured transactions law have been produced by international legislative and financial organizations. The general aim of these instruments has been to modernize the law of secured credit with

<sup>1</sup> In particular, the UN Convention on the Assignment of Receivables in International Trade; UNCITRAL *Legislative Guide on Secured Transactions*.

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the assumption that harmonized modernization of the law of secured credit lowers the cost of credit. In that context, these instruments aim to assist both developing and developed economies in reforming their laws. The law of secured transactions has remained within the boundaries of domestic law with close links to the law of property, contracts and insolvency, where the law represents cultural stance and public policy preferences that vary among States. These factors are coupled with different economic or political expectations, competition among legal systems, the tensions inherent in international law making<sup>2</sup> and the scepticism of legal practitioners towards new rules and adapting to them. For years, all of these factors have prevented a meaningful secured transactions law reform that could have successfully accompanied the globalization of financial markets. In terms of international instruments on secured transactions law, certain arguments have been put forward that some of these instruments have been influenced by a particular legal system.<sup>3</sup> While this argument may have some theoretical support, it is clear that many of the principles of international instruments on secured transactions have been implemented in national laws and derive from these laws and not from a particular system. This has been done in two ways. First, States directly implemented principles of the international texts in their domestic law; and second, States that have implemented a secured transactions law that is consistent with the recommendations of, for example, the UNCITRAL Secured Transactions Legislative Guide, have essentially implemented the principles of the Receivables Convention in their domestic law.<sup>4</sup>

It needs to be understood that law is ‘a vehicle for social change’.<sup>5</sup> At a time when a country’s social fabric, economic and financial strength are changing due to the global financial crisis and ensuing credit crunch, it is crucial to modernize the law of secured credit and respond to the needs of businesses. That can be achieved either by taking international

<sup>2</sup> See R. Goode, ‘Rule, Practice, and Pragmatism in Transnational Commercial Law’ 54 *ICLQ* 539 (2005).

<sup>3</sup> See e.g. G. McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Cheltenham: Edward Elgar, 2011).

<sup>4</sup> For more discussion on this matter see below G. McCormack ‘Secured Transactions Law Reform, UNCITRAL, and the export of foreign legal models’; S.V. Bazinas ‘The utility and efficacy of the UNCITRAL Legislative Guide on Secured Transactions’ and N.O. Akseli ‘The utility and efficacy of the UN Convention on the Assignment of Receivables and the Facilitation of Credit’, Chapters 2, 8 and 9, respectively, below.

<sup>5</sup> R. Wacks, *Philosophy of Law: A Very Short Introduction* (Oxford University Press, 2006), p. xii.

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instruments as an example, adapting their rules according to the needs of domestic law and legal tradition, or looking at other comparator jurisdictions and taking example from their experiences. This is obviously not something that can be done overnight. It can only be achieved with a clear remit, inclusion of all interested parties and on an incremental basis. If the law responds to the needs of businesses, this will not only be significant for the economic growth of a country, but also indicative of the fact that the country's law is regarded as an influential example or suitable for exportability to overseas law reform activities.<sup>6</sup>

The ability to give security influences not only the cost of credit but also, in some cases, whether credit will be available at all. The difficulties posed by inefficient secured credit laws are felt acutely in both advanced and emerging economies as a result of financial crisis. Businesses have expectations from the law<sup>7</sup> and the State has a responsibility to establish a financial and legal framework which understands the barriers to access to finance, and either addresses those barriers or enables businesses to negotiate them. In emerging or developing markets, unpredictable and poor secured credit laws deter international financial organizations and banks from extending credit and investing in those countries. In developed markets, inefficient secured transactions laws hinder further economic growth. Arguably, increasing the availability of credit and lowering its cost contributes to international and domestic economic development. It is believed that international instruments on secured transactions law aim to provide predictability and modernized rules which will have a positive impact on the availability and cost of credit and can be influential and taken as helpful examples in the domestic law reform activities. International standards set by international legislative bodies and financial organizations have the necessary merit to achieve this.

The collection encompasses essays from a broad range of perspectives in order to contextualize the availability of credit and secured transactions law reform: from the role of banks in economic development and financial crises (Bholat); from the facilitation of credit and political and policy

<sup>6</sup> For similar lines of argument, see R. Goode, 'Insularity or Leadership? The Role of the United Kingdom in the Harmonization of Commercial Law' 50 *ICLQ* 751 (2001).

<sup>7</sup> See 'Secured Transactions Law: The Case for Reform' available at <http://securedtransactionsproject.wordpress.com/case-for-reform/> (last accessed 12 January 2013). It is submitted that the Secured Transactions Law Reform Project is an excellent platform to discuss the inefficiencies of secured transactions law and unpick the shortcomings of the current secured transactions law in England, and a basis to reform the law incrementally in a way that responds to the needs of businesses in the twenty-first century.

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perspectives (McCormack); from the position of international financial institutions (Bazinas and Dahan); from the involvement of international organizations and the impact of this on the law and the market (Halliday); from UNCITRAL's legislative texts (Bazinas and Akseli); and from the domestic perspective of the secured transactions law reform in England (Raymond). The volume's conclusions present a clear view of the efficacy and utility of international legal standards and their impact on making the credit available and secured transactions law reform in a time of crisis (Beale). The comments under each part (Gray, Mistelis, Gabriel and McGrath) reflect critical perspectives.

Part I of the collection focuses on the availability of credit, challenges in access to credit, and the problems in harmonizing and reforming the law by adopting a specific model. Taking the role of banks in economic development and financial crises with particular reference to their loan portfolio in Britain in the period leading up to and following the Great Recession as the starting point for his analysis, David Bholat, in his chapter 'Money, bank debt, and business cycles: between economic development and financial crises', looks at the role conventionally attributed to banks in economic theory and history. Bholat focuses particularly on Joseph Schumpeter, who draws a distinction between economic growth and economic development on the basis of the presence or absence of banking. He then presents a more sceptical story based on Friedrich Hayek's theory, which tends to depict banks as uniquely problematic institutions in the making of financial crises. Finally, Bholat offers some UK data on the behaviour of banks leading up to and following the current crisis. In particular, the relative growth in net lending secured on real estate, among other evidence, casts doubt on their role in economic development, indicating instead their centrality to what has been described as 'financialization'. In his chapter, 'Secured transactions law reform, UNCITRAL and the export of foreign legal models', Gerard McCormack, develops his earlier argument that modernization does not equal a liberalization agenda and subjects it to greater scrutiny. In this novel treatment, McCormack analyses the effects of recognizing security rights. He criticizes the harmonization of the law of secured credit, particularly in the 'liberal' American-nuanced way that the UNCITRAL Guide seeks to do. He then considers why 'liberal' secured credit regimes are considered to be beneficial. Moreover, McCormack addresses in greater detail critical perspectives on the international harmonization and modernization agenda. He concludes against the secured transactions reform in the American-oriented manner that the Guide seeks to effect. Joanna Gray, in her contribution in

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Part I of the collection, stresses the interplay between the ability to create security, increased financialization and the banking crisis of 2008.

Part II of the collection considers the role and interest of international financial institutions and international organizations in setting standards on secured transactions for robust financial systems in emerging economies and credit facilitation. In his chapter, 'International organizations as global lawmakers: seven shifts in practice for secured transactions law and beyond', Terence Halliday undertakes an in-depth analysis of the impact of law on the market by questioning why international organizations produce standards. Halliday analyses four theories (professional, ecological, realist and idealist) in responding to why international organizations and financial institutions develop standards. He then develops his argument into how and whether they should produce standards and suggests seven shifts in international organizations' orientation and practices. These include comparing private international financial institution lawmaking to public international organizations' lawmaking, naive developmentalism to contingent developmentalism, unexamined theories to tested theories, arbitrary exemplars to alternative models, narrow disciplinary to broad inter-disciplinary, globalized localisms to normative options, static norms to recursivity. In his initial chapter, 'The creation of international commercial law standards by international financial institutions: why they do it and whether they should', Spyridon Bazinas discusses the examples of overlap between international legislative bodies and the international financial institutions in producing international legal standards on secured transactions law. Bazinas suggests that international financial institutions should coordinate their efforts with international legislative bodies to continue their economic development mandate and could focus on the economic analysis of law to achieve an efficient law reform. Frederique Dahan, in her chapter, 'The power of secured transactions law and the challenge of its reform', analyses the philosophy that the EBRD, as an international financial institution, has applied in its work in the field of secured transactions reform. Dahan states that this philosophy is based on two important elements in secured transactions law and law reform: the facilitative objective of the secured transactions law should be made legally efficient, and secured transactions law is versatile and the law reform should embrace that versatility. She maps out the EBRD's work in reducing the credit risk in a legally efficient manner by analysing the Core Principles for secured transactions law. The chapter then progresses to the EBRD's recognition of secured transactions' versatility. Dahan concludes that the secured transactions law reform will

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continue, and that in this process the EBRD's legal efficiency criteria in law reform will be a useful device. In his chapter, 'Commentary on the involvement of international financial institutions in secured transactions law reform', for effective law reform, Loukas Mistelis suggests a stronger cooperation between international financial institutions and international legislative bodies.

Part III of the collection considers the UNCITRAL *Legislative Guide on Secured Transactions* and the UN Convention on the Assignment of Receivables in International Trade. These two texts and their general principles provide a valuable tool for legislators in their law reform efforts. Spyridon Bazinas in his chapter, 'The utility and efficacy of the UNCITRAL *Legislative Guide on Secured Transactions*', analyses, in great depth, the effectiveness of the UNCITRAL *Legislative Guide on Secured Transactions* ('the Guide') in reducing the cost of credit. The chapter systematically looks at the key policy issues of the Guide in addition to the soft law approach adopted by it. Bazinas concludes by responding in detail to the critique of the Guide. In his chapter, 'The utility and efficacy of the UN Convention on the Assignment of Receivables and the Facilitation of Credit', Orkun Akseli discusses the general principles of the UN Convention on the Assignment of Receivables. Akseli's argument is that modern rules that efficiently endorse receivables financing are critical in reducing the cost of credit and have the potential to increase cash flow and further investment in the face of financial crisis. These rules may be used as a starting point in domestic law reform activities. Henry Gabriel, in his chapter, focuses on the soft law nature of the Guide and on the factors that make the Receivables Convention less successful than expected.

Part IV of the collection focuses on whether and the extent to which international standards set by international standard-setting bodies and financial organizations may be used to help reform the law of credit and security. The particular significance of this theme is that with the collapse and quasi-nationalization of banks in the UK, apart from a reform in banking regulation, it is necessary to achieve the reform of the law of credit and security to facilitate access to credit. In her chapter, 'How may international standards assist law reform in England?', Anjanette Raymond provides an analysis as to why there is a need for reform in secured transactions law in England. She considers law reform efforts in England and the ultimate failure of the reforming initiative. Her chapter finally suggests modernization of English personal property security law. Noel McGrath, in his chapter, 'Commentary on the international standards and the reform of English personal property securities law', provides a

different perspective in terms of domestic law reform. McGrath comments that law reform in secured transactions law may be achieved by incremental changes.

Hugh Beale, in his concluding chapter, ‘The UNCITRAL *Legislative Guide on Secured Transactions* as a model for law reform: some conclusions’, presents the case for a secured transactions law system that could work more efficiently.